



Sacred Heart
UNIVERSITY

Sacred Heart University
DigitalCommons@SHU

WCOB Faculty Publications

Jack Welch College of Business

11-2002

The Balanced Scorecard at Philips Electronics

Andra Gumbus

Sacred Heart University, gumbusa@sacredheart.edu

Bridget M. Lyons

Sacred Heart University, lyonsb@sacredheart.edu

Follow this and additional works at: http://digitalcommons.sacredheart.edu/wcob_fac



Part of the [Business Administration, Management, and Operations Commons](#), [Business and Corporate Communications Commons](#), [International Business Commons](#), and the [Strategic Management Policy Commons](#)

Recommended Citation

Gumbus, Andra, and Bridget Lyons. "The Balanced Scorecard at Philips Electronics." *Strategic Finance* 84.5 (2002): 45-49.

This Article is brought to you for free and open access by the Jack Welch College of Business at DigitalCommons@SHU. It has been accepted for inclusion in WCOB Faculty Publications by an authorized administrator of DigitalCommons@SHU. For more information, please contact ferribyp@sacredheart.edu.

Performance Measurement

The following article is the
third in a three-part series
featuring companies
that have implemented the
balanced scorecard.

THE BALANCED SCORECARD AT PHILIPS ELECTRONICS

IT'S USED TO ALIGN COMPANY VISION,
FOCUS EMPLOYEES ON HOW THEY FIT
INTO THE BIG PICTURE, AND EDUCATE
THEM ON WHAT DRIVES THE BUSINESS.

BY ANDRA GUMBUS
AND BRIDGET LYONS



When a management tool becomes popular, it's only logical to question whether it's a fad or the future. One performance measurement tool—the balanced scorecard (BSC)—has broad appeal. Approximately 50% of *Fortune* 1,000 companies in North America and about 40% in Europe use a version of the BSC, according to a recent survey by Bain & Co. The number of software and consulting firms currently providing BSC-related products and services supports these statistics. But do companies think the BSC is here to stay? Philips Electronics does. This worldwide conglomerate has gathered its more than 250,000 employees in 150 countries around the card because it sees this tool as the future—not a trendy tool. The key benefit for Philips: Management can streamline the complicated process of running a complex international company with diverse product lines and divisions. Here's how it cascades throughout the organization.

ILLUSTRATION: ROBERT PIZZO/ROBERTPIZZO.COM



Reproduced with permission of the copyright owner. Further reproduction prohibited without permission.

The drive to implement the balanced scorecard at Philips Electronics came from the top down—as a directive from the Board of Management in Europe to all Philips divisions and companies worldwide. The directive went to each of the companies and their quality departments, with the effort in the medical division headed by the Quality Steering Committee that reports to the president of Philips Medical Systems. (Later we'll look specifically at the experiences of the Philips Medical Systems North America (PMSNA).)

Philips Electronics has used the balanced scorecard to align company vision, focus employees on how they fit into the big picture, and educate them on what drives the business. An essential aid to communicating the business strategy, the BSC works as a vehicle to take key financial indicators and create a quantitative expression of the business strategy. In fact, Philips Electronics' management team uses it to guide the quarterly business reviews worldwide in order to promote organizational learning and continuous improvement.

THE ROAD TO IMPLEMENTATION

Philips' underlying belief in creating their balanced scorecard is that understanding what drives present performance is the basis for determining how to achieve future results. With this understanding in mind, Philips designed the scorecard to provide a shared understanding of the organization's strategic policies and vision of the future. Their operating principle in the design was to determine factors that were critical for achieving the company's strategic goals.

The tool has helped Philips Electronics focus on factors critical for their business success and align hundreds of indicators that measure their markets, operations, and laboratories. The business variables crucial for creating value, which are known as the four critical success factors (CSFs) on the Philips Electronics BSC, are:

Competence (knowledge, technology, leadership, and teamwork),

Processes (drivers for performance),

Customers (value propositions), and

Financial (value, growth, and productivity).

Here's how these critical success factors came to life at the company.

Top-level scorecard criteria are the driving determinant for lower-level scorecard criteria. Philips wanted to make implicit assumptions about the way the business creates value explicitly through CSFs. In other words, the goal was to translate assumed relationships such as customer

satisfaction and product sales into critical success factors to measure performance. To do so, they identified which financial and customer CSFs give a competitive edge, and then they determined the process CSFs that have the greatest impact on the financial and customer CSFs giving the company that edge. Competence CSFs deliver required process, customer, and financial results.

To express the strategy in measurable objectives, the team established a performance management system that measures progress toward the corporate vision. This system links short-term actions with long-term strategy so employees understand how their day-to-day activities help achieve the company's stated goals.

In order to focus employees on the few vital goals and business priorities, the BSC cascades down throughout the organization. Top management initially deployed the BSC by setting annual operational targets, which were brought down through organizational layers as goals for the divisions worldwide and objectives at the business unit level. By deploying top-level CSFs throughout the organization, goals can be clearly linked to the business strategy as well as to all employees.

The Philips Electronics balanced scorecard has three levels. The highest is the strategy review card, next is the operations review card, and the third is the business unit card. In addition, the plan is to implement another level of the card—the individual employee card—in 2003.

The corporate quality department created specific guidelines for metric linkage for the entire company. These guidelines state that all top-level scorecard critical success factors for which the department is responsible must link metrically to lower-level cards. Three criteria were established to accomplish this. The first is inclusion: Top-level CSFs must be addressed by lower-level CSFs to achieve top-level metric goals. The second is continuity: Critical success factors must be connected through all levels, and lower-level measurements shouldn't have longer cycle times than higher-level measurements. The third criterion is robustness: Meeting lower-level CSF goals must assure that higher-level CSF goals will be met or surpassed. Goals in all card levels align with goals in the next level above, and goals become fewer and less complex as you drill down through the organization.

THE BSC AT WORK IN THE BUSINESS UNITS

At the business unit level, critical success factors were developed for each of the four perspectives of the card—competence, processes, customers, and financial. They established guidelines for the deployment of CSFs at low-

er levels in the company, stating that departments must select CSFs for which the department has a major control responsibility. These CSFs—key BSC indicators—monitor the implementation of the business strategy.

The management team of each business unit reached consensus on which CSFs distinguish the business unit from the competition. They used a value map to derive customer critical success factors by analyzing customer survey data that reflected perceived performance relative to the price for competing products. Process CSFs were derived by determining how process improvements can deliver customer requirements. Competence CSFs were identified by determining what human resources and competencies were required to deliver the other three perspectives of the card. Standard financial reporting metrics were used as financial CSFs.

The next step was for each business unit to determine key indicators at the business unit level that measure critical success factors. Assumptions about relationships between processes and results were quantified and performance drivers determined. Targets were then set based on the gap between present performance and desired performance for the current year plus two and four years in the future. The criteria: Targets must be specific, measurable, ambitious, realistic, and time-phased. Targets are derived from an analysis of market size, customer base, brand equity, innovation capability, and world-class performance.

Examples of indicators at the business unit level include:

FINANCIAL

Economic profit realized
Income from operations
Working capital
Operational cash flow
Inventory turns

PROCESSES

Percentage reduction in process cycle time
Number of engineering changes
Capacity utilization
Order response time
Process capability

CUSTOMERS

Rank in customer survey
Market share
Repeat order rate
Complaints
Brand index

COMPETENCE

Leadership competence
Percentage of patent-protected turnover
Training days per employee
Quality improvement team participation

In cascading the card down from the organizational level to the business unit level, six key indicators consistently came to the forefront for all business units:

- ◆ Profitable revenue growth,
- ◆ Customer delight,
- ◆ Employee satisfaction,
- ◆ Drive to operational excellence,
- ◆ Organizational development,
- ◆ IT support.

These six key drivers relate to each other as well as to the balanced scorecard's four critical

success factors. Organizational

development and IT support

drive the competence per-

spective; customer delight

and employee satisfaction

drive the customer per-

spective; operational

excellence drives the

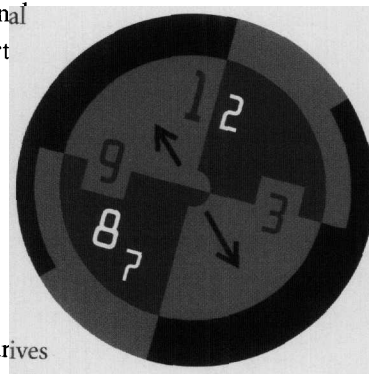
process perspective; and

profitable revenue growth drives

the financial perspective. And each

quarter the BSC metrics are used as the reporting format

for the review of each business unit's performance.



SUCCESSSES AND CHALLENGES

Although there are many successful implementations at the Philips companies, let's look at the implementation of the balanced scorecard at Philips Medical Systems North America (PMSNA). It served as an alignment tool to focus on their strategic intent to become a \$1 billion company by the year 2001.

It simultaneously guided a cultural change effort to increase accountability for results. Eventually the BSC is expected to replace the monthly accountability calls to the field office where sales are reported against forecasted numbers. Another success for the card within this division is the creation of an operational scorecard for action planning and tracking results in real-time: Data are automatically transferred from internal reporting systems and fed into the online BSC report, which is immediately accessible and contains the new results. An upcoming enhancement to customer service and satisfaction reporting will be the automatic feed of data gathered by the Gallup Organization into the online BSC report in a similar fashion.

Finally, implementing the card responded to common questions raised in the annual employee motivation survey, such as "How does what I do every day fit into the

bigger picture of the company?" The balanced scorecard enables employees to understand exactly what they need to do on a daily basis in order to impact results.

Chris Farr, former vice president of quality and regulatory at PMSNA and who was responsible for the BSC, says that companies must get buy-in to the metrics and share measures quarterly with all employees in order to succeed. "Management must give full access to their employees," Farr says. "The metrics must be shared and visible."

To share the metrics with employees, Philips Electronics uses traffic-light reporting to indicate how the actual performance compares with the target. Green indicates meeting target, yellow indicates in-line performance, and red warns that performance is below target. The visibility of results using a traffic-light model means ease-of-use with quick, easily recognizable metrics. Philips Medical Systems employs Lotus Notes-based online reporting using a system they call Business Balanced Scorecard On-Line (BBS ON-Line).

Farr said the balanced scorecard's primary strength is gaining the commitment and participation of management and employees regarding company objectives. "Employees have helped to create measures that are meaningful to customers and to the business," he says. "In this process, employees have analyzed what makes the business successful and gained a greater understanding of the business enterprise."

Other strengths include:

- ◆ The BSC promotes the sharing of best practices and creates a communication system worldwide. Each element of the card has an owner whom employees can contact to share success strategies and product fixes. BSC fosters communication, collaboration, and problem solving.
- ◆ The BSC supports a company's cultural change to a learning organization by creating a common knowledge base. If a metric is in the red zone, the employee can quickly access how to fix potential problems and avoid repeating others' mistakes, saving time and money in problem solving.
- ◆ The BSC represents an enhancement to the current "Yellow Pages" in use at Philips. Out of a total workforce of more than 250,000, roughly 22,000 employees have chosen to share project knowledge and interests on a voluntary basis using the Philips Yellow Pages. Employees



working on similar projects can communicate successes and pitfalls using the Yellow Pages on the employee intranet. The BSC takes the concept further with a defined owner accountable for each element on the card.

Other lessons Philips Electronics learned include:

- ◆ Software for use in capturing and transferring data to a BSC in real time should be selected carefully and researched fully prior to implementing the balanced scorecard. Many commercial products are available, and Philips Electronics uses a Lotus Notes-based reporting system they call Business Bal-

anced Scorecard On-Line for Web-based reporting.

- ◆ A balance must be reached to maintain visibility for employee access while maintaining confidentiality of company results that are sensitive and proprietary.
- ◆ In trying to determine employee-level performance indicators, the team learned that many critical success factors can't be directly impacted by employees.

FAD OR FUTURE?

The use of a balanced scorecard as a strategic tool represents an opportunity for an executive team to align their company to the strategic intent. Since the BSC represents a fundamental change in how an organization is measured and held accountable for results, it also poses threats to an established corporate culture and has potential weaknesses if it isn't executed properly. Yet the balanced scorecard is a powerful strategic tool—not the latest management fad—for strategic planning, goal setting, goal alignment, and measurement. No other tool provides the ability to balance all aspects crucial to business performance in 2002 and beyond. ■

Andra Gumbus, Ed.D., is an assistant professor in the management department at Sacred Heart University in Fairfield, Conn., and can be reached at (203) 396-8271 or gumbusa@sacredheart.edu. She is the former director of training and development at Philips Medical Systems North America.

Bridget Lyons, DPS, is assistant professor in the finance department at Sacred Heart University in Fairfield, Conn., and can be reached at (203) 365-7673 or lyonsb@sacredheart.edu.